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October 28, 1996

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BY HAND DELIVERY

Mr. William Caton
Office of the Secretary
Federal Communications Commission
1919 M Street, Room 222
Washington, D.C. 20554

Re: Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996

Dear Mr. Caton:

Please find enclosed for filing the original and fourteen copies of the RBOC Payphone Coalition's Opposition to Petitions for Reconsideration. I also include an electronic version as requested by the Commission.

Enclosed please find an extra copy for date-stamp.

Sincerely,

Michael K. Kellogg

Michael K. Kellogg

Enclosures

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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C.

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In the Matter of		
Implementation of the Pay Telephone	)	
Reclassification and Compensation	)	CC Docket No. 96-128
Provisions of the	)	
Telecommunications Act of 1996	)	

THE RBOC PAYPHONE COALITION'S OPPOSITION TO PETITIONS FOR RECONSIDERATION

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October 28, 1996

TABLE OF CONTENTS

EXECUTIVE SUMMARY

Although the parties to this proceeding, with a fair degree of consistency, applaud the Commission's Report and Order, a number of them have returned to the Commission to seek changes that will benefit their own private interests. The Commission's order, however, is generally well-reasoned and equitable. The RBOC Payphone Coalition therefore urges the Commission to reject most of the petitions for reconsideration.

I-A. While several interexchange carriers ask the Commission to exclude certain categories of calls from compensation -- each carrier seeking to exclude the category of calls it carries most -- none have undermined the Report and Order's reasoning or results. 0+ calls from RBOC payphones are properly included where no compensation otherwise would be paid with respect to those calls, as the statute requires fair compensation for each and every call; nowhere does it include an exception for RBOC payphones or 0+ calls. And the Commission had full authority and properly justified its decision to include international calls.

B. The interexchange carriers' contention that the Commission should rely on cost rather than market forces to calculate "fair" compensation likewise should be rejected. First, a return to outdated cost-based methodologies would permanently mire the Commission in rate regulation in an otherwise competitive industry. In contrast, by linking compensation on 1-800 and access code calls to local rates, the Commission ties per-call compensation to a competitive, market-based measure. Second, the use of the cost-based approaches could lead to a severe reduction in the number of payphones available for public use, contrary to Congress's directive to promote the widespread deployment of payphones. Third, despite the contentions of the interexchange carriers, reliance on market-based pricing will not result in overcompensation. The local market is structured to operate competitively, and the one-year transition period allows the Commission to ensure that pricing is competitive. Moreover, the Commission's reliance on the rate for local calls will, if anything, produce a per-call compensation rate that is artificially low.

C. Nor is the Commission required to reconsider the methodology for interim compensation. The Commission properly excluded from that requirement those carriers with so little volume that the costs of including them outweighs the benefits.

II. The Commission also did not err in deregulating the rate for local payphone calls. The Commission had jurisdiction to do so, properly found deregulation in the public interest, and gave fair notice that local payphone rates were at issue in this proceeding.[1]

III. The Commission properly rejected requests that it impose a set use fee or that it require coin deposits to make calls to 800 subscriber numbers. There is no reason to require a set use fee, as carriers can add a separate line item to their bills if they wish to do so, and mandating implementation of a set use fee would increase transaction costs. Similarly, requiring coin deposits would increase transaction costs -- as well as frustrating the public's expectations.

IV. With respect to reassignment of payphone assets and asset valuation, the APCC has not shown that the Commission's decision was ill-conceived. To the contrary, the plain language of the statute supports the Commission's decision to apply its existing Computer III safeguards, and nothing in the legislative history overcomes that plain language. Moreover, the APCC utterly fails to show that applying existing rules will adversely affect consumers or the market.

V. Finally, the Commission's decision on public interest payphones is unassailably sound. The Commission's criteria enable the states to place payphones where the market would not meet public needs, while ensuring that regulation does not interfere with the operation of a competitive marketplace.

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[1]NYNEX and Bell Atlantic adhere to their initial positions on these issues.

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C.

In the Matter of

Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996	))))	CC Docket No. 96-128

THE RBOC PAYPHONE COALITION'S OPPOSITION TO PETITIONS FOR RECONSIDERATION

Most of the parties to this proceeding applaud the Commission's Report and Order for its pro-competitive and deregulatory approach. Despite this widespread support, however, many commenters have returned to the Commission to ask for modifications that will promote their own private interests. Few of these petitions for reconsideration raise issues that the Commission has not fully considered in the Report and Order, and fewer still provide any basis for questioning the Commission's well-justified decisions. As a result, the vast majority of petitions for reconsideration should be rejected out of hand.

I. PER-CALL COMPENSATION [¶¶ 48-76]

A. The Statute Calls For Compensation on All Completed Calls

The Commission has imposed a requirement of per-call compensation for each and every completed call made from a payphone, so long as the market otherwise would not provide compensation. Seeking to upset that requirement, MCI -- but not AT&T or Sprint -- objects to paying RBOC PSPs per-call compensation on 0+ calls, even where the RBOC PSPs otherwise would not receive *any* compensation for originating those calls. See MCI Pet. at 4-5 (objecting to Report and Order ¶ 53). But Section 276 requires full and fair compensation on "each and every" completed call from a payphone. Because RBOC PSPs would receive no compensation with respect to many 0+ calls absent Commission intervention, the Commission was required to order per-call compensation on those calls.

Attempting to evade this unavoidable statutory mandate, MCI argues that requiring the payment of per-call compensation will violate Section 276(b)(3) by *interfering* with its contracts with location providers, which cover 0+ calls. But MCI does not argue that the compensation requirement precludes it or location providers from complying with these contracts. Nor does it contend that the contracts have somehow been nullified or voided. Instead it argues that the contracts will be less profitable, hardly the sort of thing that constitutes improper interference.

More fundamentally, MCI misconstrues Section 276(b)(3). In effect, MCI attempts to convert that provision into an exception to Section 276(b)(1)(A)'s requirement of fair compensation for each and every call. But Section 276(b)(3) has nothing to do with the fair compensation requirement. Instead, it was designed to ensure that *Section 276(b)(2)(D)* -- which gave all PSPs the right to negotiate with location owners over interLATA and intraLATA carrier selection -- would not be read as *releasing* location providers from existing contracts.[2] Consequently, MCI's attempt to twist this unambiguous grandfathering clause into an exception to fair compensation must be rejected.[3]

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[2]See S. Conf. Rep. No. 230, 104th Cong., 2d Sess. 158-59 (1996) ("Section 274(b)(1)(D) also makes it possible for independent payphone service providers, as well as BOCs, in all jurisdictions, to select the intraLATA carriers serving their payphones. However, existing contracts and agreements between location providers and payphone service providers, interLATA, or intraLATA carriers are grandfathered. Location providers prospectively also have control over the ultimate choice of the interLATA and intraLATA carriers in connection with their choice of payphone service providers"); H. Rep. No. 204, 104th Cong., 1st Sess. 88 (1995) ("Section 274(b)(1)(D) [of the House version of the Act] removes th[e] prohibition [against BOC selection of interLATA carriers on their payphones]. Section 274(b)(1)(D) also makes it possible for independent payphone service providers, as well as BOCs, in all jurisdictions, to select the intraLATA carriers serving their payphones. However, existing contracts and agreements between location providers and payphone service providers, interLATA, or intraLATA carriers are grandfathered.").

[3]Cable & Wireless, Inc. (at 15-16) urges the Commission *not* to treat regenerated phone calls (*i.e.*, multiple calls made using the # key) as additional phone calls. C&W does not dispute that treating these regenerated calls as multiple calls is both sensible and fair from an economic perspective -- or that treating them as one call leads to absurd results. But it does argue that the particular technology it employs makes it impossible for C&W to comply. However, C&W never explains why it is impossible for it to compensate PSPs for each regenerated call when it undoubtedly bills *its own customers* for each regenerated call. Moreover, C&W has a year to comply with the order; if it cannot come up with an economically viable way of handling this issue in that period, it should seek a waiver to permit it to use an algorithm or proxy in place of actual multiple call tracking.

Joined by Sprint but not AT&T, MCI also argues that international calls should be excluded from per-call compensation. MCI Pet. at 6; Sprint Pet. at 13-14. Both carriers raised this same argument in the original comments, and repeating it on reconsideration has not made it any stronger.[4]

Finally, not to be out-done by the self-serving pleadings of the interexchange carriers, certain PSPs urge the Commission to enhance compensation in their particular industry segment. Specifically, inmate payphone providers ask the Commission to impose a $0.90 per-call charge on inmate payphone calls, and to pre-empt certain state regulations. See Inmate Payphone Provider Services Coalition Pet. at 6-13 ("Inmate Coalition"); Invision Telecom, Inc. Pet., *passim*. In the Coalition's view, no special rules -- favoring or disfavoring inmate PSPs -- are required. And review of state pricing regulation of inmate payphones is at this point premature. State payphone rules will be subject to review at the state level over the next few months and, absent appropriate action from state authorities, such rules can be brought before the Commission by way of complaint.

B. The Commission's Reliance on Local Call Rates to Establish Per-Call Compensation Does Not Overcompensate PSPs

Recognizing that basing per-call compensation on an estimate of costs would embroil the Commission in the never-ending process of rate regulation in an otherwise competitive industry, the Commission declined to establish a per-call compensation rate by regulatory fiat. Instead, the Commission noted that the "most appropriate way to ensure" the "fair compensation" required by Section 276 in a competitive marketplace is "to let the market set the price for individual payphone

[4]Thus, while MCI appears to argue that requiring compensation will render international settlements unprofitable, it provides not a single example of an international call that could not support the $0.35 surcharge and still leave MCI a profit. Moreover, AT&T -- a company with no shortage of experience in international carriage -- actually supported compensation on international calls in its initial comments. In any event, as the Coalition already has explained, any costs associated with $0.35 of compensation on payphone-originated international calls can be taken into account when negotiating settlement rates. Reply Comments of the RBOC Payphone Coalition at 4 n.4. Sprint's related argument (at 13-14) that the Commission lacks authority to require payment of compensation on international calls is clearly wrong. Although the statute may not expressly *require* the Commission to impose per-call compensation on international calls, it nowhere *prohibits* the Commission from requiring compensation.

calls," Order ¶ 49. The Commission then achieved this result by linking per-call compensation on access code and subscriber 800 calls to rates for competitively-priced local calls.

Although the RBOC Payphone Coalition believes that this linkage produces compensation that is too low, see pp. 6-8, infra, it cannot deny the inescapable benefits that the linkage produces (provided, of course, that the Commission retains its decision to deregulate the local coin rate, see pp. 12-16, infra). After the interim compensation period ends, prices will be set by the give-and-take of competition in the marketplace, and not by cumbersome, costly, and highly uncertain cost proceedings in the administrative arena.

Reluctant to rely on competition when they are purchasers rather than providers, the interexchange carriers now urge the Commission to abandon this market-based approach and to return to regulatory costing models. But a return to outdated cost-based methodologies is precisely what the Commission should avoid. First, cost-based measures are inappropriate in an area, such as payphones, where the market is structured to function effectively. Second, the use of any of the cost-based approaches will lead to a severe reduction in the number of payphones available for public use -- precisely the result that Congress prohibited. Third, despite the contentions of the interexchange carriers, reliance on market-based pricing will not result in overcompensation. To the contrary, the Commission's reliance on the rate for local calls will, if anything, produce a per-call compensation rate that is artificially low.

1. *Reliance on Cost-Based Pricing in Competitive Markets is Inappropriate.*

The primary thrust of the interexchange carriers' argument is that the Local Competition Order, which established "TELRIC" pricing for interconnection and network element charges, requires the Commission to rely on a calculation of average incremental costs in the context of payphones. See, e.g., MCI Pet. at 3; AT&T Pet. at 6-15. Whatever the merits of the TELRIC approach taken in the Local Competition Order, it is entirely out of place in the context of payphones.

As an initial matter, the statutory standards are entirely different. The statutory standard in the Local Competition Order requires that interconnection and network element charges be "based on . . . cost." See 47 U.S.C. § 252(d)(1). The applicable statutory standard here, in contrast, states that the Commission's per-call compensation plan must ensure that all PSPs "are fairly compensated for each and every completed intrastate and interstate call using their payphone." 47 U.S.C. § 276(b)(1)(A). There is thus a fundamental difference between these standards. Section 251 calls for a cost-based standard. Section 276 calls for fair compensation, which appropriately looks to market-based factors (including value) to determine the price the parties would agree upon in a free and unfettered marketplace.

More fundamentally, the application of cost-based measures is wholly inappropriate where market forces can be relied upon to determine the proper measure of compensation. Section 252 governs access to local exchange facilities by a new entrant seeking to compete with the incumbent LEC that controls those facilities. Under those circumstances, the Commission concluded, the new entrant should be able to take advantage of the incumbent's economies of density, connectivity and scope. Here, by contrast, we are dealing with a competitive industry. There are many payphone providers, and Section 276 seeks to deregulate payphones to allow competition to work. Cost-based pricing methodologies may be appropriate to regulated industries, but not to competitive ones.[5]

Finally, even if cost-based pricing is appropriate where the purchaser of the service is acting as a competitor of the seller, here the IXCs are not competitors of the PSPs. Instead, they are seeking to purchase a service from the PSPs so that they in turn can offer a valuable service to their own customers. Market-based pricing is particularly appropriate in such circumstances and, indeed, already occurs for independent PSPs with respect to 1+ and 0+ traffic. As the Commission noted in its NPRM (at ¶ 16), such negotiated compensation is, by definition, "fair compensation." Indeed, the

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[5]It is for this reason that MCI's assertion (at 3) about "bottleneck" services is wholly inapposite. The payphone market is competitive, and MCI assertions to the contrary are, as explained below (pp. 8-10, infra) without merit.

interexchange carriers surely would not argue that *their* customers are entitled to buy long-distance service from them at some Commission-determined measure of incremental cost. Yet they offer no persuasive reason why PSPs should be treated differently.

2. *Reliance on the Cost-Based Approaches Suggested by the IXCs Would Dramatically Reduce the Number of Payphones Available for Public Use.*

In any event, relying on cost-based pricing here could dramatically reduce the number of payphones -- in direct contravention of Congress's command that the Commission "promote the widespread deployment of payphone services to the benefit of the general public." 47 U.S.C. § 276(b)(1). According to the interexchange carriers, the Commission should rely on some measure of average cost, usually the nationwide or regional average of long-term incremental cost of all payphones. But compensation for the "average" cost incurred would be insufficient to support the half or more of all payphones that are below average, resulting in the removal of both "high-cost" and "low-volume" payphones.[6] The Commission acted properly in selecting a market-based compensation figure that will not undermine Congress's directive to promote the widespread deployment of payphones.

3. *The Commission's Market-Based Rates Do Not Result in Overcompensation.*

At bottom, the interexchange carriers' pleas for a return to Commission-mandated regulated pricing are based on a fundamental premise -- that market-based rates will be too high -- that is demonstrably wrong. If anything, linking per-call compensation to local rates will produce rates that are *too low* compared to what a free and open competitive market otherwise would produce.

a. One need look no further than the portion of the market that *does work* to see that this is so. Currently, market forces determine the commissions paid for 0+ calls, as the delivery of those calls is freely negotiated between PSPs and carriers. In this free market, the average price for the

[6]RBOC Payphone Coalition Comments at 14 (July 1, 1996); Why "TELRIC" Is Not An Appropriate Methodology For Determining Per-Call Compensation from Payphones, Aug. 29, 1996 (attached to Ex Parte Letter from Michael K. Kellogg to William F. Caton (Aug. 29, 1996)).

delivery of 0+ calls exceeds $0.90 cents. See RBOC Payphone Coalition Comments at 10; see also id. at 11. Given that interexchange carriers are willing to pay an average of $0.90 for these calls on the free and open market, their purported astonishment at the Commission's order -- which will produce prices in the range of $0.35 -- is simply incredible. Indeed, the $0.35 per call (or less) that is likely to be produced is substantially lower than the $0.40 per call established by the Commission in 1992. See Second Report and Order, Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation, 7 FCC Rcd 3251, 3257 (1992).[7]

Indeed, if anything, linking per-call compensation to the local rate systematically results in undercompensation. This is true because local calling volumes are more sensitive to *absolute* changes in price than are long-distance calling volumes. An absolute increase of, for example, a dime on a local call represents a substantial percentage change in price (in the range of 40 percent). Because such a dramatic percentage change in price will profoundly influence demand, there is substantial pressure not to alter the local rate in such an increment. In contrast, an extra dime on a long-distance call would represent a relatively small change in price (perhaps 5 percent) and thus would have a negligible effect on demand.

Based on these different dynamics, rational actors in a fully competitive market would avoid depressing demand for local calls by loading costs into long-distance prices -- and the interexchange carriers would end up paying *more* than the local rate as compensation for use of PSP phones.[8] By

[7]AT&T's contention (Pet. at 9) that reliance on local rates "leads to a 650% increase in the compensation payable to independent payphone providers" thus is entirely disingenuous. The Commission's order actually decreases compensation on a per-call basis by 12.5 percent from 1992 levels, and even more in real (inflation-adjusted) terms. The only thing that has increased is the volume of 1-800 and access code calls -- an increase that AT&T encouraged and profits from.

[8]See RBOC Payphone Coalition Comments at 16-17; Strategic Policy Research, Economic Report on FCC Resolution of Payphone Regulatory Issues, 33-34 (attached to Comments of BellSouth Corp. (July 1, 1996)) ("SPR Report"). The demand for local payphone service is more elastic for at least one additional reason. The decision on whether or not to make the call often depends on whether the customer has sufficient coins, or the right coins, in pocket. In contrast, almost all long-distance payphone calls are alternatively billed, making the question of whether the caller has coins on hand irrelevant. Ibid.

linking interexchange prices to local rates, however, the Commission's order prevents PSPs from using this pricing mechanism and favors interexchange carriers with lower prices than the market otherwise would offer. Given that the interexchange carriers are the beneficiaries of this intervention rather than its victim, their vitriolic protestations about compensation are wholly out of place.[9]

b. Perhaps aware of this, the interexchange carriers also attempt to argue that prices in the local market will not be constrained by competition. Inflated prices in the local marketplace, they assert, will in turn lead to inflated prices for interexchange carriers. These assertions, however, are wholly unwarranted and entirely premature.

First, the payphone marketplace is competitively structured, as the Commission already has observed. Not only are there low barriers to entry and exit, see Order ¶¶ 11-19, 70, but payphone operations are increasingly threatened by the expansion of wireless technology, the basic price of which has fallen into the same range as traditional public telephone service.

This is not a matter of theory but established fact. There are already thousands of independent PSPs in the market. Their share of the number of competitive payphones in the various regions covered by the RBOC Payphone Coalition ranges from 38-59%. Ex parte Letter of Michael K. Kellogg to Michael Carowitz, Attachments (Aug. 15, 1996). And their share of newly installed payphones exceeds that of the RBOCs, and by an increasing margin each year. Id. Once payphones are fully deregulated, this competition can only intensify.

Several states, relying on these competitive forces, have deregulated payphones. And, contrary to the dire predictions of the interexchange carriers,[10] the bogeyman of supra-competitive pricing has

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[9]The benefits enjoyed by the carriers from the connection with local rates more than offset any supposed "cost differences" between local calls and long-distance calls, see Sprint Pet. at 3; AT&T Pet. at 9-10; C&W Pet. at 5-6, most of which are immaterial and which, in total, reduce compensation by a few pennies at most -- pennies that would not appear in the local rate in any event, because payphones do not accept pennies.

[10]See, e.g., MCI Pet. at 3 (asserting that "consumers who use payphones" often are "captive ratepayers" who have "no available alternative to that particular phone" and who thus "have no option but to use the payphone, even if the coin rate is unacceptable").

not reared its ugly head. Indeed, the prevailing rate in those states is only $0.35 per call -- no higher than the rate in many regulated states. Order ¶ 72. Nor has the oft-cited "problem" of locational rents -- supra-competitive pricing in areas where there is not a reasonable choice among payphone providers [11] -- materialized. See Payphone Rates in Deregulated States (Aug. 30, 1996) (attached to Ex Parte Letter from Michael K. Kellogg to William F. Caton (Aug. 30, 1996)). Surely if these were serious problems rather than the constructs of industry participants seeking regulatory favoritism, there would be some evidence of abuse. Yet such evidence is resoundingly absent.[12]

In any event, the interexchange carriers' objections -- insubstantial as they are -- are hopelessly premature. The Commission has announced that it will investigate local rates and ensure that they in fact are competitively set before true, local-rate-based, per-call compensation begins. Order ¶¶ 51, 72. Moreover, the states continue to have authority to regulate prices (subject to Commission oversight) in any instance where market forces do not reasonably constrain pricing. Id. ¶ 61. It is thus hard to believe that local pricing will exceed competitive levels, or reach the unimaginable figure of one dollar per call floated by Cable & Wireless (at 7), without prompting appropriate intervention by regulatory authorities.

c. Unable to make headway in their discussions of the marketplace, the interexchange carriers (and Sprint in particular) attempt to persuade the Commission that market-based prices are excessive by comparing their own artificially inflated estimates of potential revenues with their unrealistically low estimates of costs. But these estimates dematerialize under any rational analysis.

Thus, while Sprint (Pet. at 1-2) asserts that 0+ commissions *can* reach $3,447 per phone per year, the truth is that few RBOC payphones ever will achieve such revenues. Similarly implausible

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[11]AT&T Pet. at 11-12, 14-15 (arguing that location rents are "the rule"); C&W Pet. at 6-7 (local prices may be set based on "locational monopolies"); LDDS WorldCom Pet. at 9-10.

[12]Some interexchange carriers argue that the rates in these states may not be representative because they are sparsely populated. See AT&T Pet. at 11. But pricing in these states is uniform, from the largest cities to the most isolated rural areas, suggesting that the distinction AT&T draws -- between more and less densely populated areas -- is irrelevant.

are the interexchange carriers' minimalist estimates of costs. Sprint, for example, continues to assert that it should pay only for wear and tear on the buttons of the phone, id. at 5, while AT&T unjustifiably excludes the cost of the basic payphone line and commissions from its cost estimates, AT&T Pet. at 6-7 & nn.6-7.

These tactics already have been exhaustively explored and thoroughly discredited, and nothing their proponents reassert on reconsideration is new.[13] Indeed, once these estimates are corrected for various deficiencies, they produce an *average* compensation figure -- which is by definition insufficient to support a majority of phones -- that differs only slightly from the $0.35 rate the Commission's order is likely to produce. See Andersen Reply Report at 3.[14]

C. There is No Reason for the Commission to Alter its Calculation or Allocation of Interim Compensation

Unable to mount a serious attack on the Commission's long-term compensation plan, various carriers attack the Commission's proposal for interim compensation. In particular, the larger carriers attack the Commission's plan as discriminatory, because it excludes the smallest carriers and LECs from the interim compensation requirement. See LDDS WorldCom Pet. at 4-7; AT&T Pet. at 15-18.

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[13]RBOC Payphone Coalition Reply Comments at 13-16 (July 15, 1996); Arthur Andersen, L.L.P., Critique of MCI's Use of the Hatfield Study and Other Issues 1-3 (attached to RBOC Payphone Coalition Reply)) ("Andersen Reply Report").

[14]Finally, various parties raise the internally contradictory assertions that 1-800 services will go up in price, or that they will be unable to recover payphone compensation costs. See AirTouch Pet. at 6-7; Sprint Pet. at 6. With respect to the effect on 1-800 service prices, the commenters offer nothing but speculation, and implausible speculation at that. While the number of 1-800 calls made from payphones is substantial, it is dwarfed by the enormous volume of 1-800 calls carried on the interexchange carriers' networks. Consequently, it is likely that per-call compensation will have only an imperceptible effect on 1-800 call prices, especially if carriers choose not to pass through the costs as a line-item to individual customers but instead recover them on a pro-rata basis from all customers. Similarly unsupported is Sprint's assertion that it cannot recover increased costs in connection with debit cards. First, because the Telecommunications Act of 1996 was passed in February of 1996 and anticipated long before that, Sprint long has had the opportunity to include the anticipated cost of per-call compensation in the price of the cards it sells. Second, any effect on Sprint is likely to be minimal, as the vast majority of cards sold before the order was issued will have been used or destroyed before the order even takes effect. Third, and finally, the fact that Sprint issued these cards at a time when it was getting an unjustified free-ride at the PSPs' expense is no excuse for continuing that free ride.

Contrary to the assertions of these carriers, the Commission is entitled to make distinctions among carriers where doing so makes sense. Here, the volume of 1-800 and access code payphone traffic carried by the smallest carriers and by LECs simply cannot justify the administrative expense of requiring them to pay interim compensation. Moreover, to the extent the carriers demand that LECs pay interim compensation on intraLATA toll calls, see AT&T Pet. at 16-17, there is no evidence in the record concerning the number of intraLATA toll calls made per payphone per month, and the number is likely to be minimal in any event. If interim compensation on intraLATA toll calls were considered important, the carriers should have raised this issue and created a record before this late date in the proceeding.

Finally, AT&T (at 17-18) argues that the interim rates overcompensate low-usage and semi-public payphones. This is both true and irrelevant. The average volume figure *will* generate too much compensation on low-volume phones. But it also will produce *too little* compensation on high volume phones -- precisely offsetting the excess payments of which AT&T complains. It is thus difficult to understand what AT&T is complaining about. Besides, this "income averaging" effect has (in the short term) a salutary side-effect: It delays for the interim period the removal of otherwise unprofitable phones, permitting the states both to identify the public interest phones they want to keep and to arrange funding for them.[15]

II. LOCAL COIN CALLS [¶¶ 55-62][16]

A number of states attack the Commission's decision to deregulate local coin rates following a one-year transition to a fully competitive market. Some argue that the Commission lacks jurisdiction to issue such an order. See, e.g., Office of the People's Counsel for the District of

[15]AT&T's contention that PSPs will *install* additional phones just to get one year's worth of compensation is -- in light of the *thousands* of dollars of investment required to place each phone -- simply absurd.

[16]NYNEX does not join with the Coalition in this section relating to local coin calls, but instead adheres to the position it took in the initial Coalition Comments.

Columbia Pet. at 5-6 ("OPC-DC"); Joint Petition of Maine, et al., at 3-8 ("Joint Petition"); NYDPS Pet. at 4-6; Ohio PUC Pet. at 7-8. Others urge the Commission not to exercise that authority on the grounds that deregulation is unwise and will harm consumers. California PUC Pet. at 2, 4; Okla. Corp. Comm'n Pet. at 2-3; Texas PUC Pet. at 4-6. Still others argue that the Commission has violated the Administrative Procedures Act by failing to provide adequate notice of its intention to deregulate. Joint Petition at 16-17; NYDPS at 2-4.

1. The argument that the Commission lacks jurisdiction is incorrect.[17] As the Commission has already noted, it has an express statutory obligation "to ensure that the compensation for all local coin calls is fair." Order ¶ 56. Moreover, the statute states that "to the extent that any State requirements are inconsistent with the Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements." 47 U.S.C. § 276(c).

The Joint Petitioners (at 5) argue that the language of the statute is in fact ambiguous and that "'[c]ompensation' and 'compensation plan' must be understood as terms of art that refer only to compensation between owners of payphones and carriers not to the 'compensation' paid by end-user consumers who deposit coins in payphones for the purpose of making local calls." See also NYDPS at 5. But Congress directed the Commission to ensure fair compensation on "each and every completed intrastate and interstate call." It did not require that all such compensation come from interexchange carriers, and Congress was surely aware that many payphone calls are local coin calls and therefore do not involve interexchange carriers at all. By requiring the Commission to ensure fair compensation on *all* calls, Congress plainly contemplated that the Commission would pass regulations affecting local coin rates.[18]

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[17]Bell Atlantic adheres to the position taken in its original comments on this issue. Comments of Bell Atlantic at 1-2 (July 1, 1996).

[18]The Ohio PUC (at 7) attempts to rely on a passage from the Senate Report on S. 652 as an indication of Congress's desire not to interfere with state regulation of rates charged to end users. See S. Rep. No. 23, The Telecommunications Competition and Deregulation Act of 1995, 104th Cong., 1st Sess. 58 (1995). But the Conference adopted the House version of the payphone

2. The claim that deregulation of local coin rates is bad policy is equally misguided. These states assume that the payphone market is "inherently dysfunctional." Ohio PUC at 5. But there is no basis for that assumption. The fact that local telephone companies have long provided payphone service as part of their "basic service," see OPC-DC at 8, is precisely what Congress sought to change when it required the Commission to remove payphone subsidies from basic exchange and exchange access revenues. It has no bearing on whether payphone service, like CPE before it, will be fully competitive once payphone assets are taken out of the rate base and deregulated.

As already explained, pp. 8-10 supra, there is ample record support for the Commission's conclusion that the "payphone industry has the potential to be very competitive." Order ¶ 11. And the Commission adequately identified and either eliminated or found insufficiently substantial the potential obstacles to such competition. Id. ¶¶ 14-19. Under these circumstances, the Commission was plainly correct that "full and unfettered competition is the best way to achieve Congress' dual objectives to promote 'competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public.'" Order ¶ 55 (quoting 47 U.S.C. § 276(b)(1)). Allowing market forces to work "will lead to the more efficient placement of payphones, improved payphone service, and lower prices for consumers." Id.[19]

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provision, not the Senate version. See Conf. Report, supra note 1, at 159 ("The conference agreement adopts the House provision with some modifications and a clarification"). The Senate version of the payphone provision (found in Section 311 of S.652) did not contain either the Commission's mandate to ensure compensation on each and every intrastate call or the express preemption authority granted by Section 276(c). The House Report by contrast notes that, under the House version, "[i]n place of the existing regulatory structure, the Commission is directed to establish a new system whereby all payphone service providers. . . are fairly compensated for every interstate and intrastate call made using their payphones." H. Rep. No. 204, supra note 1, at 88.

[19]It is worth stressing that the Commission's decision to deregulate the local coin rate is tempered by the one-year transition period during which states may continue to set the local coin rate. Order ¶ 60. The Commission has also provided "an exception to the market-based approach for states that are able to demonstrate to the Commission that there are market failures within the state that would not allow market-based rates." Id. ¶ 61. This measured approach fully addresses any concerns expressed by the states.

Claims that deregulation of the local call rate will harm consumers are not only entirely speculative, they are, in fact, directly contradicted by the record evidence. Five states already have deregulated local coin rates and prices have not risen dramatically in those states. The rate is \$.35 per call in four of the states, and only \$.25 per call in the fifth. See p. 9, supra. Even more important, there is no evidence of locational rents being charged. Local coin rates are uniform in each of these states. See p. 9, supra.

The Commission correctly found that "existing local coin rates are not necessarily fairly compensatory." Order ¶ 58. The Commission has a statutory obligation to ensure that local coin rates are fairly compensatory. Moreover, adequate local coin rates are critical to the statutory decision to remove subsidies. Allowing the market to set local coin rates is the fairest and most efficient procedure, and the most in keeping with Congress's intent to deregulate the industry. Equally important, the deregulation of the local coin rate is critical to the Commission's plan for per-call compensation on dial around and 800 access code calls. If the local coin rate is not deregulated, then the whole industry will continue to be subject to pervasive regulation, contrary to Congress's intent and to sound policy.[20]

3. The claim that the Commission failed to give adequate notice that it was considering deregulating the local coin rate is frivolous. All Section 533(b)(13) requires is that a notice of proposed rulemaking provide notice of "either the terms or substance of the proposed rule *or a description of the subject and issues involved*" (emphasis added). The Commission's NPRM clearly identified the local coin rate as a critical issue, and the possibility that the Commission would choose to deregulate that rate was clear from the outset. As the Commission explained:

> Section 276 of the Act requires the Commission to ensure that the payphone provider receives fair compensation for each interstate and intrastate call, including local coin sent-paid calls. Section 276 also expressly preempts state regulations that are inconsistent with

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[20]The Ohio PUC's suggestion (Pet. at 5) that states be allowed to cap the rates would, of course, completely defeat the idea of letting rates be set by market forces -- and would do nothing to redress the fact that many states currently mandate non-compensatory rates.

our regulations. We seek comment, however, on how we should exercise our jurisdiction under Section 276.

NPRM ¶ 20. The Commission then went on to outline "a range of options for ensuring fair compensation for these calls," including setting a nationwide local coin rate or providing guidelines for the states. Although the Commission did not expressly list deregulation as one of the options in this passage, neither did the Commission suggest that its list was exhaustive. Moreover, the Commission had just noted a few paragraphs earlier its tentative conclusion that market-based compensation is inherently "fair compensation." Id. ¶ 16.

Certainly, the Commission was under no obligation to adopt the precise proposals contained in its NPRM,[21] and the deregulation of the local coin rate was a "logical outgrowth," American Federation of Labor v. Donovan, 757 F.2d 330, 338 (D.C. Cir. 1985), of the Commission's obligation to ensure "fair compensation" on local calls and its conclusion that market-based compensation is fair compensation. Numerous parties, *including some of the state petitioners here*, addressed this precise question in their comments.[22]

Equally unavailing is the claim of the Joint Petitioners (at 9-10) that the Commission's decision not to regulate (i.e., to let market forces govern) the local coin rate is a decision to forbear under Section 10 of the Act, 47 U.S.C. § 160, and that the Commission must therefore make the specific findings required in that section. Section 10 applies to Commission decisions not to apply existing regulations and statutory provisions to particular carriers or services. Here, the Commission is promulgating the regulations that will apply to payphone services, as it was directed to do under Section 276. Section 10 simply has no relevance to that process. In any event, in the course of its

[21]Trans-Pacific Freight Conference v. Federal Maritime Commission, 650 F.2d 1235, 1249 (D.C. Cir. 1980), cert. denied, 451 U.S. 984 (1981) ("The whole rationale of notice and comment rests on the expectation that the final rules will be somewhat different -- and improved -- from the rules originally proposed by the agency.").

[22]See, e.g., CalPUC Comments at 13 (July 1, 1996); New York City Dep't of Info. Tech. and Telecomm. Comments at 9 (July 1, 1996); New York State Dep't of Pub. Serv. Comments at 3 (July 1, 1996) ("NYPDS").

decision, the Commission did plainly conclude that market forces were sufficient to ensure just and reasonable rates, to protect consumers, and to promote the public interest. Order ¶ 55.

III. ADMINISTRATION AND TRACKING

A. The Commission Correctly Selected a "Carrier-Pays" System [¶¶ 77-87]

In its Report and Order, the Commission recognized that a carrier-pays system places the payment obligation on the primary economic beneficiary of the call -- the carrier over whose facilities the call is routed. Order ¶ 83. On reconsideration, Sprint and AT&T have argued for a "set use" fee system, under which the carrier collects the cost from the end-user through a separate line on the bill, but passes the amount collected through to the PSP. Sprint at 14; AT&T at 18-19. As an initial matter, it is hard to see what changing to a set use fee would accomplish. Under the carrier-pays rule adopted by the Commission, carriers can effectively convert "carrier pays" into a set use fee *themselves* simply by passing costs through to customers as separate line items on their bills. The only effect of requiring a set use fee is to convert this otherwise optional cost-recovery method into a mandatory one.

Moreover, requiring carriers to impose a set use fee (outside of those areas that already have adopted them) will impose unnecessary transaction costs on market participants. See Order ¶ 84. AT&T's own figures support the Commission's conclusion in this respect. In California, which currently uses a set use fee, AT&T currently keeps 4 cents out of each 25 cent "set use" fee to cover "billing and collection expenses." AT&T at 20 n.30. While 4 cents per call may not seem much at an individual level, the aggregate impact of this cost is staggering. By AT&T's own estimate, it carves out over 16 percent of the amount it collects to cover transaction costs. Applied nationwide and to all carriers, these fees would result in transaction costs in the millions, if not tens of millions, of dollars.

Rather than seeking the imposition of a set use fee to be assessed against customers in carrier bills, PCIA and PageMart argue in favor of imposing a set use fee that requires would-be callers to deposit coins into the payphone. Both argue that payphone callers expect to deposit coins in payphones and that a caller-pays system would in no way decrease the number of payphone calls. PageMart Pet. at 2; Personal Communications Indus. Ass'n. Pet. at 3. But this would be extremely inconvenient for callers. It is precisely to *avoid* the deposit of coins that many 800 numbers, like 800 numbers that operate as access codes, were created. Moreover, requiring coin deposits would not only leave customers "surprised" and "burdened," AirTouch Pet. at 5, but would artificially depress the demand for 800 calls from payphones. As AirTouch itself points out, if "consumers would stop using payphones to dial 800 numbers . . . [t]he logical result could be reduced payphone usage and therefore a reduction in payphones. It is inconceivable that this would be in the public interest." Id. at 15. Because of the adverse effect a caller-pays system would have on consumer welfare, the Commission correctly rejected it. Order ¶ 85.[23]

Finally, some petitioners propose that PSPs should allow payphone users to reach subscriber 800 calls that the carrier has elected to block so long as the payphone user deposits coins. AirTouch Pet. at 14-16; PageNet Pet. at 21-23. To allow such coin-deposit bypass of carrier blocking, however, PSPs and LECs would have to design a line that, although identifiable as a COCOT line under most circumstances, ceases to be identified as such (and appears to be a normal business line) once coins are deposited into the phone. Such a modification to the LEC network would be prohibitively expensive, if it could be accomplished at all.

B. Call Tracking [¶¶ 98, 113]

In its Report and Order, the Commission mandated that LECs identify payphones by a distinct code (07 or 27) within the ANI. Order ¶ 98. Both AT&T and MCI propose that the Commission put some teeth behind this requirement by denying compensation to PSPs who fail to pass the

[23]Still other commenters suggest increasing the SLC to compensate PSPs for the use of their payphones. PageMart Pet. at 2-3; PCIA Pet. at 9-11. But this is entirely contrary to the purpose of the statute. Section 276 was designed to *free* the payphone marketplace of subsidies, not to shift them from one area (the CCLC) to another (the SLC).

payphone coding digits. MCI Pet. at 9; AT&T Pet. at 23. The Coalition agrees with this position in principle. While it is not the PSP that must provide the special ANI codes -- it is the LEC -- LECs cannot provide these codes unless the PSPs use COCOT line services. Accordingly, the Commission should clarify that, if a PSP does not use COCOT line services, it will not be eligible for compensation. See RBOC Payphone Coalition Petition for Clarification 6-7.[24]

IV. ASSET VALUATION AND REGULATORY SAFEGUARDS

A. The Commission Need Not Reconsider Its Decision to Permit Integrated LEC Payphone Operations to Rely on Existing Cost Allocation Rules [¶¶ 161-171]

The APCC urges the Commission to require RBOCs to *transfer* payphone assets to a separate set of books at "going concern value" whether or not the RBOC creates a separate payphone affiliate. APCC Pet. at 7. But the APCC's arguments in support of this unprecedented change in the Commission's accounting rules are wholly unconvincing. The plain language of the statute clearly dictates that the Commission's existing accounting safeguards -- which allow payphone costs to be allocated to unregulated activities at net-book value -- are legally appropriate, and the legislative history is not to the contrary. Moreover, the APCC nowhere explains how or why Congress (or any rational person for that matter) would intend the counter-intuitive result the APCC seeks. Indeed, the APCC's pseudo-economic justification for extending "going concern valuation" to integrated payphone operations not only fails to advance the APCC's cause, but demonstrates the irrationality of applying "going concern valuation" even to assets that are transferred to a separate affiliate.

[24]MCI's further proposal that LECs be required to pass digits distinguishing between LEC and non-LEC payphones, MCI at 8, has no conceivable legitimate purpose. Whether the payphone is a LEC's or not bears not at all on compensation or even fraud prevention; these causes are served by identifying the payphone, which the ANI does, not by revealing the payphone's owner. Moreover, implementing these specific identification codes would require widespread and costly changes to LEC switches, with no countervailing benefits. Similarly unnecessary are the requests that non-equal access payphones, and calls made to 950 numbers, be required to provide ANI digits. Given the relatively insignificant number of calls affected, it is simply not worth the expense of making the required adjustments.

1. *There Is No Evidence That Congress Intended the FCC to Require Payphone Assets to Be Maintained on a Separate Set of Books.*

Consistent with sound accounting practice and its own Part 64 rules, the Commission has decided that, where RBOCs choose to run their payphone operations on an integrated basis, they need not establish a separate set of "payphone books." Instead, they are required to allocate costs between regulated and unregulated operations on their existing books. Order ¶ 163. At the same time, the Commission determined that RBOCs that choose to operate their payphone operations as a separate affiliate must transfer assets at "fair market value" consistent with Part 64. Id. ¶ 164.

Seeking to force RBOCs to conduct a "fair market" valuation of their assets whether or not a separate affiliate is used, the APCC argues that Section 276 *requires* RBOC PSPs to transfer payphone assets to a separate set of payphone books. APCC at 7-15. But the APCC's analysis begins and ends with an isolated snippet of legislative history, and does not make so much as a passing reference to the text of the statute. This error is fatal: It is well-established that "[i]f the statute is clear and unambiguous, 'that is the end of the matter, for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.'" Atlanta College of Medical & Dental Careers, Inc. v. Riley, 987 F.2d 821, 827 (D.C. Cir. 1993) (quoting Board of Governors of the Federal Reserve Sys. v. Dimension Fin. Corp., 474 U.S. 361, 368 (1986)).

Here, Congress expressed its intent in unmistakable and unambiguous statutory language. Under Section 276, the Commission is expressly authorized to employ its existing Computer III accounting safeguards, which do *not* require the transfer of unregulated operations to a separate set of books. As the statute declares, the Commission must impose "nonstructural safeguards for Bell operating company payphone service," including accounting safeguards that, "at a minimum, include the nonstructural safeguards equal to those adopted in the Computer Inquiry-III (CC Docket 90-623) proceeding." There can be no dispute that the Commission's decision is entirely consistent with that language. In fact, the Commission employed precisely the Computer III accounting safeguards referenced as acceptable in the statute.